

# MCC and Indonesia: Investing in Innovation for Sustainable Economic Growth

The five-year, \$600 million MCC compact with the Republic of Indonesia is designed to reduce poverty through economic growth. The compact's three projects are expected to increase household income in project areas through increased productivity, reduced energy costs, and improved provision of public sector growth-enhancing goods and services.

## Green Prosperity Project

The majority of Indonesia's poor live in rural areas that are rich in natural resources, but over-extraction and inadequate management of these resources threaten Indonesia's ability to sustain high rates of economic growth and reduce poverty. One in seven villages in Indonesia does not have access to reliable and affordable electricity, and many more rely on expensive and dirty diesel generation. Illegal logging, conversion of land for agriculture, water pollution, and other unsustainable land use practices adversely affect the natural assets that people rely on for their livelihoods and well-being.

Protecting Indonesia's natural resource base in the face of demographic, social, and economic forces requires developing viable economic alternatives. The compact's \$332.5 million Green Prosperity Project is designed to increase productivity and reduce reliance on fossil fuels by expanding renewable energy, and to increase productivity and reduce land-based greenhouse gas emissions by improving land use practices and management of natural resources.

These objectives support the Government of Indonesia's commitment to reducing greenhouse gas emissions and developing corridors of economic growth within its medium- to long-term development plans.

The Green Prosperity Project will provide technical and financial assistance for projects in renewable energy and natural resource management to raise rural household incomes. This is expected to reduce reliance on fossil fuels, improve land management practices, protect natural capital, and complement efforts to reduce emissions from deforestation and environmental degradation.

## Community-Based Health and Nutrition to Reduce Stunting Project

Currently, over one-third of children under five years old in Indonesia experience stunted growth, as measured by international standards of height for age. Consequences of nutritional deprivation in a child's early life include higher infant and child mortality, increased susceptibility to infection and illness, reduced adult physical stature, and impaired cognitive abilities, all of which result in long-term economic losses to individuals and society.

The compact's \$131.5 million project seeks to reduce and prevent low birth weight, childhood stunting, and malnourishment of children in project areas. The project will target approximately 7,000 villages in provinces where rates of stunting and low birth weight in infants and children up to two years old are higher than national averages.

Drawing on a growing body of international evidence on interventions to reduce stunting and low birth weight, the project provides an incentives-based scheme to increase demand for tools to reduce stunting, while improving the health sector's capacities to respond to increased demand. The project builds on existing community engagement mechanisms tested under a community-driven pilot program, *Generasi*, which successfully supported community efforts to improve targeted health, nutrition, and education indicators.

## Procurement Modernization Project

Efficient and effective public procurement is a strategic public sector function and a fundamental component of good governance. Indonesia's existing public procurement systems are highly vulnerable to fraud, waste, and abuse, resulting in significant loss of funds and diminished quality of goods, works, and public services. A recent study by the Corruption Eradication Commission estimates that in 2011 alone, the equivalent of over \$15 billion could be misused due to corrupt and inept procurement practices.

The Government of Indonesia has taken significant steps, however, to modernize its public procurement system. The National Public Procurement Policy Agency charged with implementing these modernization efforts will use MCC assistance to promote improved practices in public procurement.

The \$50 million Procurement Modernization Project is designed to assist the Government of Indonesia in achieving significant government expenditure savings with no loss—or an increase—in the quality of procured goods and services. The project includes activities to build a career path for procurement civil servants, create an institutionalized role and structure for procurement professionals that provides sufficient authority to implement good practice, and provide procurement professionals with new skills and tools to conduct procurements.

## Compact Administration

The compact includes approximately \$75.8 million for administrative and oversight costs, including the cost of project administration, management, auditing, fiscal and procurement agent services, and environmental and social oversight. The cost of compact monitoring and evaluation is budgeted at \$10.2 million.

## Expected Results

The **Green Prosperity Project** is expected to benefit households and businesses in the project's targeted districts primarily through expanded access to renewable energy and improved natural resource management. Improved land use practices may also indirectly benefit other public and private stakeholders downstream or adjacent to Green Prosperity Project provinces or districts. Economic rates of return for sub-projects will be determined during due diligence of proposals submitted for funding to the Green Prosperity Project's investment facility. MCC requires a minimum return of 10 percent.

The **Community-Based Health and Nutrition Project** is expected to benefit up to 2.9 million children and their families in up to 7,000 villages by developing human capital to support increased lifetime incomes. The preliminary estimated economic rate of return for this project is 13 percent.

The **Procurement Modernization Project** will initially support improved performance of 30 Procurement Service Units that are being established in central ministries and local governments. Subject to the terms and conditions of the compact, the project will then scale up the most successful models—those which achieve economic rates of return exceeding MCC requirements—of up to an additional 70 units. Residents and businesses located in and with economic relationships in the targeted districts will benefit, in addition to people benefitting from the public goods and services procured by participating national level ministries. This project's groundbreaking nature is expected to allow the Government of Indonesia to contribute to the international community's latest thinking on the benefits of procurement reform. The first phase of the project will develop systems to quantify the benefits; in order to proceed with phase two, the compact will require planned activities to have an economic rate of return above 10 percent.